

Internal Revenue Service
Director, Exempt Organizations

Department of the Treasury
P.O. Box 2508 - EP/EO
Cincinnati, OH 45201

Date: AUG 08 2001

Employer Identification Number:
[REDACTED]

DLN:
[REDACTED]

Person to Contact - I.D. Number:
[REDACTED] - [REDACTED]

Contact Telephone Numbers:
[REDACTED] Phone
[REDACTED] FAX

CERTIFIED MAIL

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth.

The evidence presented disclosed that the organization was incorporated on [REDACTED] in [REDACTED].

The purposes for which the corporation was formed are as follows:

- A. Plan, develop, and sponsor, produce educational media and related materials and programs to promote interracial unity.
- B. To cooperate, contract, enter into venture agreements, and to offer whatever aid and assistance to educational institutions, religious organizations, local, state and federal government agencies, private agencies, foundations, business institutions and individuals to promote the purposed enumerated herein.
- C. The corporation shall have and may exercise in furtherance of its corporate purposes all of the powers specified in [REDACTED], the powers specified in [REDACTED], and the power to land to which it has legal title.
- D. To deal and engage in any activity allowed under the provisions of [REDACTED] and permissible within the Internal Revenue Code Section 501(c)(3) and any other provisions thereof.

The information submitted in your Form 1023 application indicates that your primary activity is assisting non-profit organizations that are currently exempt under section 501(c)(3) of the Internal Revenue Code by providing them with promotional media materials. Your professional video production promotes the exempt organizations' operations and helps raise funds to support their operations.

Your stated sources of financial support will consist of revenues from the performance of activities including the sale of videos produced in connection therewith, grants and contributions from general public.

Your fundraising program will primarily generate its income through establishing contracts with other non-profits to deliver media and related services at cost substantially below those of for profit companies. It will also derive income from the sale of educational materials that it develops on various projects. You state you will occasionally apply for grants to fund its program initiatives. You also state you do not presently have plans to engage in soliciting the general public for funds though it may do so sometime in the future.

You have also stated in the application that in instances where you charge for services and products, it will be on the basis of cost plus 5% to 10% service fee. The service fee will go to support your operating budget.

Section 501(c)(3) of the Internal Revenue Code provides, in part, for the exemption from Federal income tax of organizations organized and operated exclusively for charitable, religious, scientific or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

In order to qualify under Internal Revenue Code 501(c)(3), an organization must be both "organized" and "operated" exclusively for one or more purposes specified in that section. If the organization fails to meet either the organizational test or the operational test, it is not exempt. (Regs. 1.501(c)(3)-1(a)(1)). The organizational test relates to the rules for governing an organization and the purposes stated in its articles of organization. The operational test relates to the organization's activities.

Section 1.501(c)(3)-1(b)(1)(i) of the Regulations provides that an organization is organized exclusively for one or more exempt purposes only if its articles of organization limit the purposes of such organization to one or more exempt purposes; and do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the Regulations states that an organization will be regarded as "operated exclusively" for one or

more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(2) of the Regulations provides that the term "charitable" includes relief of the poor and distressed, advancement of education and science and the promotion of social welfare designed to accomplish any of the above purposes.

Section 1.501(c)(3)-1(d)(3) of the Regulations provides, in part, that the term "educational" relates to the instruction of the public on subjects useful to the individual and beneficial to the community. Museums and schools are included in the examples of educational organizations which, if they otherwise meet the requirements of section 501(c)(3) of the Internal Revenue Code, may qualify under this section.

In Revenue Ruling 76-4, 1976-1 C.B. 145, an otherwise qualifying organization that produces and distributes free (or at small cost-defraying fees) educational, cultural, and public interest programs for public viewing via public-educational channels of commercial cable television companies is operated exclusively for educational purposes and is exempt from Federal income taxes under section 501(c)(3) of the Code.

In Revenue Ruling 71-529, 1971-C.B. 234, an organization providing investment management services to other exempt organizations at substantially below cost was held to be exempt under section 501(c)(3) of the Internal Revenue Code.

In Revenue Ruling 72-369, 1972-2 C.B. 245 provides that an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations does not qualify for exemption under section 501(c)(3) of the Internal Revenue Code. The ruling emphasizes that an organization is not exempt merely because its operations are not conducted for the purpose of producing a profit. Further, providing such services on a regular basis for a fee is trade or business ordinarily carried on for profit. The fact that the services are provided at cost and solely for exempt organizations is not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Internal Revenue Code. Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable.

In *B.S.W. Group, Inc. v. Commissioner*, 70 TC 352, Dec. 35, 1975, the tax court held that a Corporation that planned on offering consulting services for a fee, to a non-profit, limited resource organizations

engaged in various rural-related activities was not entitled to tax-exempt status because it did not operate exclusively for charitable, educational or scientific purposes. In addition, the court determined that the taxpayer had completely failed to show that its own services, or the services performed by its consultants, would not be in competition with commercial businesses such as personnel agencies, consulting referral services, real estate agents, housing rental services, banks, loan companies, trash disposal firms or environmental consulting companies.

Your organization is distinguished from the organizations described in Revenue Ruling 71-529 and Revenue Ruling 76-4, because your organization does not provide services at substantially below cost or producing and distributing free (or at small cost defraying fees) educational, cultural, and public interest programs, respectively.

However, your primary activities are similar to the activities of the organization described in Revenue Ruling 72-369 and B.S.W. Group Inc. in that you are essentially a professional video production on the basis of cost plus █% to █% service fee. The fact that you are organized on a non-profit basis and provide services primarily to exempt organizations is not determinative of exempt status. Providing professional video production on a regular basis for a cost plus █% to █% service fee is characteristic of a trade or business ordinarily carried on for profit. As stated in Revenue Ruling 72-369, the provision of such services for a fee at no more than cost is not an exempt activity under section 501(c)(3) of the Internal Revenue Code.

An organization is not exempt merely because its operations are not conducted for the purposes of producing a profit. To satisfy the "operational test" the organization's resources must be devoted to purposes that qualify as exclusively charitable within the meaning of section 501(c)(3) of the Internal Revenue Code and applicable Regulations.

In addition, your organization is primarily conducting an activity indistinguishable from an ordinary commercial enterprise.

Accordingly, this organization's activities are not charitable and therefore the organization does not qualify for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Internal Revenue Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a Trust, or Form 1120 if you are a corporation

or an unincorporated association. Contributions to you are not deductible under section 170 of the Internal Revenue Code.

Contributions made to you are not deductible by the donors as charitable contributions as defined in section 170(c) of the Internal Revenue Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that:

A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely,

Steven Miller

Director, Exempt Organizations

Enclosures
Form 6018
Publication 892